



Order 96-2-1

UNITED STATES OF AMERICA  
DEPARTMENT OF TRANSPORTATION  
OFFICE OF THE SECRETARY  
WASHINGTON, D.C.

Issued by the Department of Transportation  
on the 2nd day of February, 1996

**REDUCTIONS IN FISCAL YEAR 1996 FUNDING  
AND SERVICE LEVELS UNDER  
THE ESSENTIAL AIR SERVICE PROGRAM**

**Docket OST-95-889 et al.**

**SERVED: February 8, 1996**

**FINAL ORDER**

**Background**

By Order 95-11-28, November 17, 1995, the Department implemented program-wide reductions in essential air service subsidy payments and allowed for reductions in service levels, effective November 27, 1995, in response to a reduced program appropriation enacted by Congress for fiscal year 1996. The new appropriation of \$22.6 million represented a \$10.8 million reduction from the \$33.4 million that had been appropriated for the program in fiscal year 1995. Moreover, Congress indicated that all communities participating in the program in fiscal year 1995 should continue to be eligible for participation in fiscal year 1996. Consequently, the Department implemented reductions generally consisting of (a) the termination of subsidy for second-hub service, (b) the termination of subsidy for service more than five days a week, thus withdrawing support for weekend service in most cases<sup>1</sup> and (c) the termination of subsidy for more than two round trips a day. As a result, the Department reduced the level of subsidy-supported service to ten round trips a week to a single hub.

Although our decision in Order 95-11-28 was final, we invited comments from affected communities and carriers to ensure proper implementation of the reductions and to correct any errors as quickly as possible. In fact, we responded expeditiously in several instances<sup>2</sup>. In the present order, we will consider the remainder of carrier and community comments.

<sup>1</sup> However, Order 95-11-28 allowed carriers to operate some subsidy-supported weekend service in lieu of weekday service where such a schedule would best meet the needs of the community.

<sup>2</sup> See the errata to Order 95-11-28, regarding the calculation of various subsidy rates, as well as Order 95-12-3, December 4, 1995, regarding subsidized service at certain Alaskan communities.

## Comments

In response to Order 95-11-28, we received comments from three carriers: Big Sky Transportation Co., Ltd.; Great Lakes Aviation, Ltd.; and Exec Express II, Inc., d/b/a Lone Star Airlines. We also received seven sets of comments from community representatives: the City of Fergus Falls, Minnesota; joint comments from six communities in western Kansas and Lamar, Colorado; the Prowers County Board of Commissioners, on behalf of Lamar; the Maine Department of Transportation, on behalf of Augusta/Waterville, Bar Harbor and Rockland; the City of Rockland; the North Dakota Aeronautics Commission, on behalf of Devils Lake, Dickinson and Jamestown; and the Dickinson Municipal Airport Authority.<sup>4</sup> Broadly speaking, the comments address either the reductions in the levels of supported service or the reductions in subsidy paid to carriers providing those services. We will consider each of these areas in turn.

## Service Reductions

Many of the commenters request that their own communities be exempted from the reductions for any of a variety of reasons, or question the manner in which the reductions were implemented. For example, Fergus Falls asks that it be exempted because it contributes 25 percent of the subsidy supporting its service.<sup>5</sup> Big Sky states that the seven Montana communities it serves should be exempted because of their isolation from alternative service,<sup>6</sup> and the Prowers County Commissioners similarly cite Lamar's isolation. The Maine Department of Transportation points out that, because the historical levels of subsidized service differed from community to community, reducing support to ten round trips a week everywhere resulted in deeper cuts at some communities than others.<sup>7</sup> The western Kansas communities contend that support for second-hub service should have been maintained based on traditional considerations such as geographic location and traffic data. In addition, the Kansas communities request that, although the Department has reduced the levels of subsidized

---

<sup>3</sup> The six western Kansas communities are Dodge City, Garden City, Goodland, Great Bend and Hays, Kansas, and Liberal, Kansas/Guymon, Oklahoma.

<sup>4</sup> In addition, we received joint comments from the Cities of Cordova, Petersburg, Wrangell and Yakutat, Alaska, which we considered in Order 95-12-3.

<sup>5</sup> Fergus Falls and Dickinson are the only two otherwise-ineligible communities participating in the program under 49 U.S.C. 41736, which permits communities to receive federally subsidized air service if they pay 25 percent of the total subsidy required and meet certain other criteria.

<sup>6</sup> Big Sky operates subsidized service from Glasgow, Glendive, Havre, Lewistown, Miles City, Sidney and Wolf to Billings, the nearest small hub. The highway distances from the communities to Billings range from 129 to 295 miles, and all are well beyond 400 miles from the nearest large or medium hub.

<sup>7</sup> At Augusta/Waterville, for instance, the Department had been supporting four round trips each weekday and weekend, or 24 round trips a week, but reduced support to ten round trips a week -- a 58-percent decrease. At other communities (six of the seven Montana communities being examples), the Department had been supporting two round trips each weekday and weekend, or 12 round trips a week, and also reduced support to ten round trips a week -- only a 17-percent decrease.

service, the Department should view the reductions as a temporary measure for fiscal year 1996 only and refrain from revising communities' essential air service determinations.<sup>8</sup>

More fundamentally, Big Sky contends that the Department could have achieved the required program reductions by eliminating some communities from subsidy eligibility altogether while leaving intact the levels of subsidized service at the remaining communities. Big Sky characterizes the Conference Committee Report language cited in Order 95-11-28 as "vague and unclear,"<sup>9</sup> and suggests that the Department should have achieved the spending cuts by eliminating some communities from eligibility based on their proximity to alternative service, as in past program reductions.

Big Sky is incorrect in asserting that we could have achieved the spending reductions by eliminating communities. The Department has consistently advocated program cuts based on eliminating communities located near alternative service. But it is Congress, not the Department, that determines which communities are or are not eligible for subsidy under the essential air service program. Under 49 U.S.C. 41731, all communities that were eligible before October 1, 1988, and that received scheduled air service at any time after January 1, 1990, have retained their eligibility unless Congress has explicitly directed otherwise either by amending the underlying statute or by including language in the program's appropriation. Congressional appropriations language for fiscal years 1989, 1990 and 1994 contained such directives -- typically in the form of eligibility criteria -- and the Department acted accordingly.<sup>10</sup> Contrary to Big Sky's understanding, those criteria are established by Congress, not by the Department.

For the new fiscal year, Congressional appropriations language simply restated the eligibility criteria of fiscal years 1994 and 1995. Our reapplication of those criteria resulted in the elimination of one community -- Worthington, Minnesota. Without further direction from Congress broadening those criteria, we lacked the statutory authority to eliminate any others. Notwithstanding Big Sky's opinion of ~~the~~ report language, the *appropriations* language simply did not give the Department the latitude to make spending cuts in the manner Big Sky would have preferred. And in our view, the report language plainly indicated Congressional awareness of the effect that the appropriation would have on the program: Congress expected the Department to support some level of service at all then-subsidized communities, and to achieve substantial spending cuts by reducing the supported service levels as necessary.

We appreciate and understand the various communities' views that their own particular circumstances justify their being exempted from any reductions. As we explained in Order 95-11-28, however, the very depth of the funding reduction required that all communities -- whether the Department pays 100 percent or 75 percent of their subsidy -- would have to share in the service cuts if all were to retain even a minimum level of viable service; the various claims of individual communities, while often reasonable when viewed separately, are incompatible when considered together. We recognize that we reduced the level of subsidized service at some communities disproportionately. For example, we reduced subsidized service at Augusta/Waterville, Maine, from 24 to ten weekly round trips, whereas we reduced

---

<sup>8</sup> Communities' essential air service determinations, which are periodically revised to reflect changing market conditions, designate the levels of service that the Department will guarantee. The determinations generally designate one or two hubs to which service should be provided, the minimum number of frequencies and available seats to be provided, and the number of intermediate stops allowed. Although Order 95-11-28 reduced the levels of service actually being supported by subsidy, it did not take any action with respect to the underlying determinations.

<sup>9</sup> The report states: "The conferees fully intend that all essential air service communities that are participating in the program in fiscal year 1995 will continue to be eligible for participation in the essential air service program in fiscal year 1996, albeit at reduced levels. The conferees expect that the Department may be required to make pro-rata reductions in the subsidy or daily/weekly service levels to manage the funding reductions included in the conference report."

<sup>10</sup> See Orders 89-9-37, September 22, 1989, which eliminated six communities under a supplemental appropriation for fiscal year 1989; 89-12-52, December 29, 1989, which eliminated another 20 under the program's fiscal year 1990 appropriation; and Order 93-11-44, which eliminated 11 more under the program's fiscal year 1994 appropriation. Congress reiterated the fiscal year 1994 eligibility criteria in the appropriations for fiscal years 1995 and 1996, and we have subsequently eliminated additional communities; see, for example, Orders 94-5-11, May 9, 1994, regarding Trenton, New Jersey; 94-10-20, October 17, 1994, regarding Danville, Illinois; and 95-8-32, August 1, 1995, regarding Danville, Virginia.

subsidized service at Wolf Point, Montana, from 12 to ten weekly round trips. Considered from another perspective, however, isolated communities, such as Wolf Point, may be more affected by service losses than communities near alternative service, such as Augusta/Waterville. Augusta/Waterville is just 71 highway miles from a small hub at Portland; in comparison, Wolf Point is 295 highway miles from the nearest small hub of Billings. Proportionate losses in service do not necessarily translate into proportionate losses in service value. Moreover, proportionate service reductions would have left some communities with just a single round trip a day -- a result that is below the statutory minimum of two round trips a day<sup>11</sup> and which, as we noted in Order 95-11-28, we wished to avoid if at all possible.

For similar reasons, we could not continue to support second-hub service at any communities. Maintaining two-hub service for some communities while still cutting spending to the required level would have necessitated reducing other communities' service to a single round trip a day to a single hub. Moreover, the underlying statute does not require that the Department support service to second hubs. Instead, two-hub guarantees have always been a matter of Departmental discretion. While market conditions at certain communities have always justified dual-hub designations under a fully funded program, we could no longer support discretionary service at such communities when severe budgetary constraints prevented us from supporting even the minimum statutory guarantees elsewhere.<sup>12</sup>

The western Kansas communities request that we characterize the service reductions as a "temporary" measure and refrain from revising communities' guarantees to reflect those reductions. In fact, we do not know whether the reductions are temporary. All that is certain

---

<sup>11</sup> See 49 U.S.C. 41732(b).

<sup>12</sup> For example, the statute guarantees two round trips a day, six days a week, but the program's funding level no longer permits us to support service more than five days a week.

is that, under the program's fiscal year 1996 appropriation, we cannot, at present, support more than ten round trips a week at each community. The immediate future of the program is entirely dependent on legislation and funding. And in any event, the current statute calls for the program to expire on September 30, 1998 -- two and a half years from now. As for communities' guarantees, we have not revised the essential air service determinations to reflect the reduced service levels that we are now supporting, nor do we plan to do so. Because current funding is insufficient to maintain service consistent with those guarantees, the relevance of those guarantees is open to question. The value of now revising them is thus also dubious.

### Subsidy Reductions

All three carriers that filed comments -- Lone Star, Great Lakes and Big Sky -- object to various aspects of the methods that the Department used to revise subsidy rates to reflect reduced service levels.<sup>13</sup>

Lone Star disagrees with our assumption that traffic and revenue would decline in proportion to the estimated decline in total operating expenses. For example, we reduced the level of supported service on Lone Star's Harrison-HotSprings-Dallas/Ft. Worth route from three round trips each week~~ly~~ and weekend to two round trips five days a week --*i.e.*, from 18 to ten round trips each week. Assuming that 20 percent of carriers' costs were fixed, we estimated that the 44-percent reduction in service would result in no decline in fixed costs, a 44-percent decline in variable costs, and thus a 36-percent decline in total operating costs.<sup>14</sup> We further assumed that traffic and thus revenue would also decline by 36 percent. If both costs and revenues decline by 36 percent, the reduction in subsidy need is also 36 percent.

Lone Star asserts that reducing service from three to two round trips a day is likely to result in a traffic decline on the order of 50 percent, rather than 36 percent as we assumed. We are not prepared to agree with that expectation. If carriers believe that reducing service from three to two round trips a day would reduce traffic by half, they should be equally prepared to accept the reverse: ~~that~~*increasing* service from two to three round trips a day will ~~double~~ traffic. Our experience has not shown this to be the case, nor would we expect it. In 1991, after Congress substantially increased program funding, the Department renegotiated subsidy rates for numerous communities in order to support three round trips a day rather than two. In no case did any carrier project that the higher service level would double traffic; in fact, few were willing to project that traffic would even increase proportionately,*e.*, by even half that amount. Furthermore, we are confident that carriers will use their marketing judgment to schedule flights when demand for service is greatest; in eliminating some flights, carriers should largely be able to eliminate those that are used least.

---

<sup>13</sup> The Department's methods are described in detail in Order 95-11-28; see pp. 4-5 as well as Appendixes A and B.

<sup>14</sup>  $.20$  [fixed costs] plus  $10/18$  of  $.80$  [variable costs] =  $.64$ , or a 36-percent reduction.

Great Lakes asks us to reconsider our adjustment of the subsidy rate covering its service at five communities in Minnesota and South Dakota -- Fairmount, Mankato, Worthington, Brookings and Mitchell. As noted earlier, Order 95-11-28 terminated Worthington's subsidy eligibility. We therefore first reduced Great Lakes' total subsidy for all five communities by one-fifth to reflect the termination of subsidy for Worthington, and then applied our methodology to the remaining subsidy to reflect reduced service at the other four communities. Great Lakes states that our approach eliminated subsidy covering fixed costs incurred at Worthington. In fact, that was our intention, since we allowed Great Lakes to suspend all service there. Station expenses, for example, represent a major component of fixed costs, and Great Lakes realized the full cost savings associated with maintaining a station by leaving the community. Great Lakes' comments do not explain why those savings should not be fully reflected in our adjustment of its subsidy rate.

As discussed earlier, Big Sky opposes any service reductions at the seven Montana communities that it serves, but we have concluded that some service reductions at those communities were unavoidable. Given those circumstances, Big Sky states that its subsidy as modified by the Department is insufficient, largely because the Department's estimate of fixed costs at 20 percent of total operating costs is, in its case, too low. The Department reduced Big Sky's total annual subsidy at all seven communities from about \$3.543 million to \$3.024 million; Big Sky estimates that an annual subsidy of \$3.240 million is appropriate.

After carefully reviewing Big Sky's comments and supporting data, we are not convinced that the carrier's subsidy rate requires further revision. Big Sky's calculations imply that more than 50 percent of its total operating expenses are fixed -- an extremely high proportion under any circumstances. However, our review suggests that the carrier is capable of achieving substantial savings beyond those that it recognizes in its comments. In particular, Big Sky currently uses four aircraft to serve the seven communities; one aircraft is devoted solely to operating two nonstop round trips a day between Sidney and Billings. Our analysis indicates that Big Sky could considerably reduce its operating costs by using three aircraft in its system, devoting one to serving Sidney, Glendive and Miles City. We recognize that this approach requires some restructuring of the current route patterns for those three communities and, in some cases, might result in schedules that are less optimal than those previously in place. In view of the severe reductions in program funding, however, some loss in service quality may have to be accepted.

This order is issued under authority delegated in 49 CFR 1.56(i).

**ACCORDINGLY,**

1. Except to the extent granted herein, we affirm our findings and conclusions set forth in Order 95-11-28, November 17, 1995; and

2. We will serve a copy of this order on the parties to the dockets listed in the Appendix.

By:

**CHARLES A. HUNNICUTT**  
Assistant Secretary for Aviation  
and International Affairs

(SEAL)

*An electronic version of this document is available  
on the World Wide Web at  
<http://www.dot.gov/dotinfo/general/orders/avation.html>*